

Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, DC 20554

In the matter of:)	
)	
Universal Service Support Mechanism)	
)	
Ex Parte Comments on Proposed Fourth Quarter 2004)	
Universal Service Contribution Factor (DA 04-2976))	
)	

CC Docket No. 96-45

The following comments are submitted in response to the Proposed Fourth Quarter 2004 Universal Service Contribution Factor (DA 04-2976) released by the Wireline Competition Bureau (“Bureau”) on September 16, 2004.

Specifically, we encourage the Commission to review the Bureau’s proposal to apply \$150 million from the collections carried over from previous quarters to lower the projected demand and the contribution required for the schools and libraries support mechanism for the upcoming quarter. We believe that reducing contributions at the same time that E-rate funding has been suspended due to a change in accounting standards is inappropriate and will be detrimental to the program. Unless the Commission takes action regarding the projections of demand and the proposed contribution factor by September 30th, the proposal will be deemed approved¹ and \$150 million in needed E-rate funding will be lost.²

COMMENTS

In its *Schools and Libraries Order*,³ the Commission adopted a proposal to carry forward (or “roll-over”) unused E-rate funds into subsequent funding years starting with the second quarter of 2003. Previously, unused funds had been used to reduce carrier contributions. Under the new roll-over rule, it was expected that quarterly carrier contributions in the Schools and Libraries funds would be fixed at \$562.5 million (1/4th of the \$2.25 billion annual program funding cap).

¹ If the Commission takes no action regarding the projections of demand and administrative expenses and the proposed contribution factor within the 14-day period following release of this Public Notice (September 16th), they shall be deemed approved by the Commission

² Unless recaptured by future contributions that exceed the \$562.5 million quarterly amount needed to maintain the \$2.25 billion annual funding.

³ *Schools and Libraries Order*, 17 FCC Rcd at 11523-24 para. 3.

In the second quarter of 2004, however, the Bureau's contribution calculation began utilizing a USAC "alternative projection of demand" that reduced the required contribution by \$200 million. The reduction in the third quarter of 2004 was another \$200 million and, as indicated above, the proposed reduction in the fourth quarter is \$150 million more.⁴ In total for 2004, this amounts to a reduction of \$550 million, almost 25% of the \$2.25 billion in new funding required for the year.

Under earlier E-rate accounting practices, such reductions may have been justified. Program disbursements can easily lag program commitments by 1-2 years. As such, the Schools and Libraries Fund was accruing what might be considered by some as "excess" cash. As of June 30, 2004, the Fund's cash balance was approximately \$3 billion.⁵ Although, in the long-term, the program was expected to require full quarterly contributions of \$562.5 million, projected quarterly disbursements in the short-term could be funded by a combination of lower quarterly contributions and a drawdown of what might be deemed an overly conservative cash balance. Essentially, the contribution reductions represented a form of cash management based on historic E-rate disbursement characteristics.

Effective October 1, 2004, however, USAC has been directed by the FCC to adopt government accounting standards. The primary effect of this change, as we understand it, is to limit existing and new E-rate commitments to cash on hand. Although cash balances are significant, so too are the remaining commitment liabilities from earlier funding years (and from the first series of waves for FY 2004). As a result, the SLD has suspended the issuance of new Funding Commitment Decision Letters ("FCDLs"). No FCDLs have been issued since August 3rd. The SLD has given no indication as to how much longer the suspension will last. Presumably, no new commitments for FY 2004 or earlier years can be made under the new accounting standards until: (a) committed, but undisbursed, funds can be reduced (a path that the SLD is pursuing vigorously); (b) new fund contributions are received; and/or (c) different accounting practices are approved.

The current funding suspension is giving a black-eye to the E-rate program and, at least indirectly, to the FCC. It is causing severe cash flow problems and/or project delays for many schools and libraries, whose applications have been processed and approved internally by the SLD, but who cannot be notified that funding is or will become available. The suspension is also generating a disturbing degree of uncertainty among applicants preparing for the FY 2005 funding cycle.

With the SLD struggling to overcome cash restrictions under the new government accounting standards, it appears highly inappropriate for the Bureau to propose another

⁴ We note that the \$150 million reduction proposed in the fourth quarter, unlike the second and third quarter proposals, is not attributed to "USAC's alternative project of demand," but appears to be a Bureau construct alone. USAC filings for the fourth quarter do not include the Supplemental Information Regarding Funding Requirements, as was provided in third quarter filings, upon which the Bureau could base an alternative demand projection.

⁵ \$ 3,081,402,378 on a cash basis; \$ 3,234,903.051 on an accrual basis.

reduction in program contributions. The stated rationale for the reduction seems to be based on the previously used, non-government accounting standards, rather than on the new government standards that have led to the funding suspension.

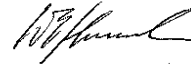
Although the continuation of contribution reductions might — to view it in its most positive light — be taken as a sign that the Bureau believes that E-rate's accounting problems can be resolved in a manner that would permit USAC to resume earlier commitment and cash flow practices, such a move seems overly optimistic in light of the current funding suspension.

SUMMARY

E-Rate Central believes that the proposed reduction in USF contributions, at a time when the E-rate program has suspended new commitments pending resolution of cash and/or accounting problems, is detrimental to both the short- and long-term prospects of the program and to the schools and libraries that rely upon it.

We urge the Commission to review and reverse the proposed E-rate funding reduction before the proposal is deemed automatically approved on September 30th.

Respectfully submitted,



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